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Bureau of Public Affairs • Department of State

Siberian Gas Pipeline and US Export Controls October 1982

Background: Planning for a large-scale Soviet natural gas pipeline to transport western Siberian gas to West European markets began in the mid-1970s as part of a triangular project involving Iran, the USSR, and West Germany. The Iranians dropped out in 1978, but the Soviets and the Europeans decided to go ahead.

The Siberian gas export pipeline is now under construction. When completed it will be 2,800 miles long, running from the giant Urengoy gas field in Siberia to the town of Uzhgorod on the Czech-Soviet border. The pipeline will be capable of delivering 2.8 billion cubic feet-per-day of natural gas to Western Europe, via Czechoslovakian and Hungarian transit pipelines. Overall, it is expected to cost $22 billion, including $7 billion in hard currency costs (mainly pipe, pipelayers, and equipment for compressor stations).

In the late summer of 1981, the Soviet Union contracted with French, West German, and Italian engineering firms to obtain much of the equipment for the pipeline. The Soviets required each European country to make available substantial export financing in order to be eligible for pipeline contracts. The financing offers by the major European export credit agencies included subsidized interest rates, in most cases under 8% at a time when interest rates ranged from 11% to more than 20%. Using this credit, the Soviets purchased power turbines, gas compressors, and monitoring, firefighting, and control equipment. Large-diameter pipe for the project was purchased and financed separately as part of the bulk orders of Western steel pipe regularly imported by the Soviets.

In late 1981 and early 1982, long-term gas supply contracts based on the new pipeline were signed between the Soviet Union and gas distribution companies in West Germany, France, Austria, and Switzerland. (A preliminary agreement also was signed with the Italian gas distribution company, but as yet it has not received government approval.) The new contracts will significantly increase West European dependence on the Soviet Union for natural gas, in some cases pushing it above 30%. Such a level of dependence on gas can be troublesome because:

- It is a fuel particularly hard to replace on short notice because of the way it is transported and stored;
- It is used increasingly in the politically sensitive residential and commercial sectors of Europe.

By the end of the present decade and after equipment credits are paid off, expanded gas exports will earn the USSR $8-$10 billion annually in hard currency. This will be a most important source of hard currency for the Soviets, possibly offsetting the expected decline in crude oil export earnings.

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US position on the pipeline: The US believes European participation in the Siberian gas pipeline project is unwise. We have repeatedly argued that:

- The resulting gas imports will cross the threshold of prudent dependence on the USSR;
- The financing that was offered amounts to a subsidy of Soviet economic development; and
- The resulting hard currency earnings will have a strategic impact by allowing the USSR to continue to import Western goods and high technology equipment, alleviating serious domestic resource contraints.

Export controls in response to martial law in Poland: In December 1981, in response to Soviet support for the imposition of martial law and the imprisonment of Solidarity officials in Poland, President Reagan announced the suspension of all licensing for export to the USSR of, among other items, US oil and gas equipment and technology. In June 1982, in light of continuing repression in Poland, the President decided to expand the oil and gas controls to prevent export to the USSR of comparable items by subsidiaries and licensees of US firms abroad.

These controls will not by themselves prevent completion of the Siberian gas pipeline, but it is estimated that full use of the line may be delayed by as much as 2 years (to 1988) and costs will be significantly higher. Using pipelines already in place, the Soviets can begin their gas deliveries in late 1984 in accordance with the new supply contracts, but delays in completing the Siberian export pipeline will lead to disruptions in Soviet domestic energy availability.

European response: European Community nations, particularly those with equipment supply and/or gas purchase contracts with the USSR, have objected to the US oil and gas controls imposed in response to events in Poland. They have objected especially to what they view as the "extraterritorial" reach of the June 1982 US oil and gas controls, and to the controls' interference with preexisting contractual obligations. These governments believe they need to diversify their energy import sources and have welcomed the employment generated by the equipment exports connected with the Siberian pipeline.

Several European countries have ordered or urged firms in their territories to disregard the US controls, and recently several shipments of US-embargoed equipment have occurred. The US Government has responded to these violations of its export controls in accordance with the law, and the Commerce Department has imposed temporary denial orders against the companies believed to be responsible for such shipments. The orders are designed primarily to deny these companies access to US oil and gas equipment and technology while the Department of Commerce continues its investigations.

Harriet Culley, Editor, 632-1208